

May 17, 2007

INVESTMENT ADVISER
ASSOCIATION

***Wrap/SMA Accounts: New Developments
and Compliance Issues***

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Wrap/SMA Accounts

- Regulators' focus on SMAs
- Advertising and marketing issues for managers
- Suitability, individualization and rule 3a-4 issues
- Best execution, trading, and investment opportunities
- ERISA issues
- New SMA products
- Disclosure, Form ADV delivery
- Recordkeeping

Regulators' focus on SMAs

- Focus on Managers – Current SEC requests
 - List of SMA programs in which clients participate
 - Name of custodian/sponsor/broker-dealer
 - Total fee charged by the sponsor
 - Terms of Registrant's compensation
 - Client assets in each program
 - A list of gifts & trips received for program participation
 - Access to due diligence on sponsors (initial & continuing)
 - Access to client suitability questionnaires
 - Access to procedures used to record client trades
 - Access to all complaint files and responses
- Coming SMA Sweep?

Advertising and marketing issues for managers

- Manager responsibilities
- Thorny issues with
 - Blended presentations
 - Backtested performance and projections
 - Related performance
- GIPS and access to sponsor records
- Comparisons to mutual funds

Suitability, individualization and Rule 3a-4 issues

- Suitability
 - SEC confusion re client specific info
 - Due diligence with ERISA accounts
- Individualization and 3a-4
 - Overselling issues
 - Reasonable restrictions

Best execution, trading, and investment opportunities

- Nature of best execution obligations
- Sequencing issues
 - Segregating SMA Trading
 - Rotation
 - Step Outs
 - Trading Last
 - Other types of tradeaways
- Information leakage concerns
- Recent “paradigm shifts”

Polling Question: Sequencing of Orders

How does your firm trade wrap accounts compared to traditional accounts?

1. Trade wrap accounts *after* traditional accounts
2. Trade wrap accounts *before* traditional accounts
3. *Rotate* trading of wrap accounts and traditional accounts randomly by automation or manually
4. *Block* or batch wrap and traditional account trades together for execution through a single broker and allocate the shares post-trade across accounts on a *pro rata* basis
5. Trade wrap accounts and traditional accounts *simultaneously* through *separate* brokers
6. Other

ERISA issues

- Due diligence
 - Authority
 - Diversification
- Affiliated sponsors

New SMA products

- ETF SMAs
- UMAs
- Model Programs
 - Adviser-client relationship
 - Disclosure issues
 - Differences between Hands-On and Model Arrangements
 - Opportunity issues
 - Performance presentations & AUM calculations

Disclosure, Form ADV delivery

- Form ADV delivery obligations
 - Delegation to sponsor
 - Records
- Special Conflicts/Disclosure issues
 - Trading
 - Leakage of holdings & trading info
 - Net trades & embedded commissions

Recordkeeping

- Access to sponsor records
- Performance backup

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